

MEMORANDUM

TO: Local School District Superintendents
Finance Officers

FROM: Kyna Koch, Associate Commissioner
Office of District Support Services

DATE: February 11, 2005

SUBJECT: Requirements for Local School District Audits

The purpose of this memorandum is to acquaint you with statutory and regulatory requirements for local school district audits and to provide information regarding resolution of exceptions.

KRS 156.265 authorizes the State Committee for School District Audits (SCSDA) to conduct audits of the financial records of local boards of education. The audits shall be performed by a Certified Public Accountant (CPA), approved by the SCSDA, and conducted according to standards established by the committee.

The audit shall cover **ALL** accounts of the board of education including activity funds at all schools and bank accounts in the name of the district's finance corporation.

Costs incurred in the audit of federal grants, the federal school food programs, and school construction accounts may, in most cases, be charged back to those funds. Determine which grants allow audit costs as an administrative expense and in what amount. Recover all possible costs from the grants, programs, and accounts. Districts receiving less than \$500,000 in Federal Funds may not charge audit costs to Federal grants but may charge other programs and accounts as appropriate.

The SCSDA shall notify the local board of education of approval or disapproval of the executed contract and the estimated amount of the audit reimbursement on or before June 1, 2005.

Please review attachment KRS 156.255 - 156.295 as you begin this process. You should obtain an engagement letter from the contracted auditor confirming the following minimum requirements are understood. You may add to this list for the particular needs of your district audit. Certain items listed below are enclosed for your review and assistance in tailoring this list.

1. Audits shall be conducted in accordance with generally accepted auditing standards; *Government Auditing Standards*, issued by the Comptroller General of the United States; the provisions of *Office of Management and Budget Circular No. A-133, Audits of States, Local Governments, and Non-Profit Organizations, Appendix I to the Independent Auditor's Contract - General Audit Requirements, Appendix II to the Independent Auditor's Contract - State Audit Requirement, and Appendix III to the Independent Auditor's Contract - Electronic Submission*.
2. The above standards require that all district audits be unqualified because the districts are all reporting according to the GASB 34 requirements. Districts that have reported the GASB 34 requirements for two years with unqualified audit reports will now be classified as low-risk.

GASB Statement No. 39 "Determining Whether Certain Organizations Are Component Units" – an amendment of GASB Statement No. 14. The provisions of this Statement are effective for financial statements for periods beginning after June 15, 2003.

Organizations that are legally separate, tax-exempt entities and that meet ALL of the criteria should be discretely presented as component units.

GASB Statement No. 40 "Deposit and Investment Risk Disclosures". Risks are the focus and investments should be organized by investment type.

- 1) Interest Rate Risk,
 - 2) Credit Risk and
 - 3) Custodial Credit Risk
3. The audit report shall be submitted electronically in any of the following formats; Text documents shall be submitted in Microsoft Word and /or Adobe Acrobat (PDF) format, spreadsheet documents are to be submitted in Microsoft Excel, and /or Adobe Acrobat (PDF) format along with one (1) paper copy, with the Auditor's signature, to this office. If submission via e-mail is not possible, the auditor can file the school district audit on diskette in one of the formats referenced. Any other problems can be directed to our office and alternate arrangements will be made. However, some form of electronic submission is required. No more than three (3) files total (text and spreadsheet) will be

accepted electronically, unless alternate arrangements are made through the Division of School Finance.

4. One (1) copy of the audit report, along with the Data Collection Form, shall be submitted by the District, directly to the Single Audit Clearinghouse, as prescribed in OMB Circular No. A-133.
5. Audit reports are due to the Division of School Finance, Kentucky Department of Education, by close of business on **October 31, 2005**. Requests for an extension, fully describing the reasons for the request, must reach this office by **October 17, 2005**.

702 KAR 3:150 requires all boards of education to submit to the Commissioner of Education, within 45 days of receipt of the final audit report, a written plan for correcting all audit exceptions noted in the report as well as those identified through routine staff review of the reports. The staff of the Division of School Finance will review corrective action plans and monitor implementation of the plans by the districts.

Finally, attached for your information and review is a calendar of significant dates in the annual audit cycle for local school districts.

If you have any questions, please contact Sydney Lawson, Audit Branch Manager for the Division of School Finance at 502-564-3846.

Attachments: KRS 156.255 - 156.295
 Calendar
 Audit Application
 Audit Contract and Appendices

cc: Tammy Page

KK:tp

ATTACHMENT

156.255 Definitions for KRS 156.255 to 156.295.

As used in KRS 156.255 to 156.295:

- (1) "Accountant" means a certified public accountant or a public accountant registered with the State Board of Accountancy.
- (2) "Board" means the board of education of a school district.
- (3) "Committee" means the State Committee for School District Audits.
- (4) "State board" means the Kentucky Board of Education.

Effective: July 15, 1996

156.265 State Committee for School District Audits.

- (1) There shall be a State Committee for School District Audits comprised of the Governor, or a person designated by him, the Attorney General, the Auditor of Public Accounts, a person designated by the Legislative Research Commission to represent the Office of Education Accountability, and the commissioner of education. The Auditor of Public Accounts shall be the chair of the committee.
- (2) The committee shall have the accounts of each board audited not less than once every fiscal year. The committee also may, at any time, cause to be made a comprehensive and complete audit of any board. Upon the written request of the state board, the commissioner of education, the Attorney General, the Auditor of Public Accounts, the Governor, or the Office of Education Accountability, the committee may cause the accounts of a board to be audited. Each audit shall cover such period of time, and shall include such auditing procedures and standards, as the committee may designate.
- (3) Audits authorized under this section are in addition to any audits contemplated under KRS 11.090, 156.200 or KRS Chapter 43.
- (4) The actual expense of any audit authorized under this section shall be borne equally by the district board of education and by the committee from funds allocated to it (no funds currently allocated).
- (5) The committee shall meet at least quarterly. Additional or special meetings may be called by the chair.

Effective: July 14, 2000

156.275 Accountant -- Selection -- Reports.

- (1) The committee shall select, to make the audit authorized under KRS 156.265, accountants who are qualified under KRS Chapter 325 and the administrative regulations promulgated by the Kentucky State Board of Accountancy.
- (2) Immediately upon completion of each audit, the accountant shall prepare a report of his findings and recommendations in such form and in such detail as the committee may prescribe. The report shall be to the committee and in such number of copies as specified by the committee. The committee shall furnish one (1) copy to the Kentucky Board of Education, one (1) copy to the district board of education to which the report pertains, one (1) copy to the chief state school officer and one (1) copy to the Auditor of Public Accounts. The district board of education shall keep a copy of the report on file in the office of the superintendent of schools of the district and the report shall be open to inspection by any interested person, subject to reasonable rules as to time and place of inspection.

Effective: July 15, 1996

156.285 Access to records -- Witnesses -- Subpoena.

- (1) The accountant shall have access to and may examine all books, accounts, reports, vouchers, correspondence files, records, money, and property of any board. Every officer or employee of any such board having such records or property in his possession or under his control shall permit access to and examination of them upon the request of the accountant.
- (2) The committee may require information on oath from any person touching any matters relative to any account that the accountant is required to audit. The committee may administer the oath, or have it done by any officer authorized to administer an oath.
- (3) The committee may issue process and compel the attendance of witnesses before it, and administer oaths and compel witnesses to testify in any of the investigations the accountant is authorized to make.

Effective: July 15, 1994

156.295 Offenses -- Penalties.

- (1) Any officer or employee of a board or any other person who prevents, attempts to prevent, or obstructs an examination by the accountant made under KRS 156.265 and 156.275 is guilty of a high misdemeanor and shall, upon indictment and conviction in the Circuit Court of competent jurisdiction, be fined five hundred dollars (\$500).
- (2) Any person who fails or refuses to permit the examination provided for in KRS 156.285 or who interferes with such examination shall be fined not less than one hundred dollars (\$100) or imprisoned in the county jail for not less than one (1) month nor more than twelve (12) months, or both. Each refusal shall constitute a separate offense.
- (3) Any person who has custody of any books, accounts, reports, vouchers, correspondence, files, records, money, and property that the accountant is authorized to examine under KRS 156.265 and 156.285 who fails or refuses when called upon by the committee for that purpose to permit the accountant to inspect any of such materials shall, upon conviction in the Circuit Court of competent jurisdiction, be fined not more than five hundred dollars (\$500) and be subject to removal as provided by law.
- (4) Any person who refuses to be sworn when required by the committee to be sworn for the purpose mentioned in subsection (2) of KRS 156.285 shall be fined not more than five hundred dollars (\$500).
- (5) Any witness called by the committee under subsection (3) of KRS 156.285 who fails, without legal excuse, to attend or testify shall be fined not more than five hundred dollars (\$500).

Effective: July 15, 1994

**ANNUAL CYCLE FOR
LOCAL SCHOOL DISTRICT AUDITS**

May 16	Current year audit contracts due.
June 1	SCSDA approval of audit contracts.
October 17	Request for Extension due.
October 31	Audit reports due. KRS 156.265
November 1 - April 30	Audit reports reviewed; corrective action plans received and monitored; audit report corrections received.
December 15 or 45 days after district receives audit report	Corrective action plans due. 702 KAR 3:150 Send to: Tammy Page 500 Mero Street 15 th Floor CPT Frankfort, Kentucky 40601
May - June	Corrective action monitoring continues.

State Committee for School District Audits

Frankfort, Kentucky

The _____ Board of Education requests the financial accounts of the Board be audited for FY 2004-2005 in accordance with the procedures adopted by the State Committee for School District Audits. The Board has chosen the firm of:

Auditor: _____ Phone #: _____

Address: _____ Fax #: _____

Address: _____ Email: _____

The cost of the audit has been estimated at: _____

If there is an increase in the audit cost from last year, please provide an explanation:

SUBMITTED, _____, 2005 _____

Board of Education

_____ Chairman

_____ Secretary

Send **THREE** (3) copies of this request and **THREE** (3) signed audit contracts no later than May 16, 2005 to:

Division of School Finance
Kentucky Department of Education
500 Mero Street, CPT 15th Floor
Frankfort, KY 40601

INDEPENDENT AUDITOR'S CONTRACT

To provide for a school district audit in compliance with KRS 156.255, 156.265, 156.275, 156.285, and 156.295, this agreement is made and entered into this _____ day of _____ 20____, between the _____ Board of Education ("BOARD"), _____, ("ACCOUNTANT"), who is a Certified Public Accountant or a Public Accountant registered with the State Board of Accountancy, and the State Committee for School District Audits (COMMITTEE).

I. DUTIES OF ACCOUNTANT

- A. ACCOUNTANT shall render an opinion on the financial statements of BOARD for fiscal year 2004-2005. The scope and nature of the audit shall be in accordance with **Appendix I** to this Independent Auditor's Contract - General Audit Requirements and **Appendix II** to this Independent Auditor's Contract - State Audit Requirements. These audit procedures are incorporated as a part of this agreement.
- B. ACCOUNTANT shall address the audit report and written comments to BOARD and to COMMITTEE. ACCOUNTANT shall deliver one (1) electronic copy of the audit report in any of the following formats: Text documents shall be submitted in Microsoft Word, and /or Adobe Acrobat (PDF) format, spreadsheet documents are to be submitted in the Microsoft Excel, and /or Adobe Acrobat (PDF) format along with] (1) signed paper copy to COMMITTEE in care of Division of School Finance, Kentucky Department of Education, no later than October 31, 2005. Both copies of the audit report must be at the Division of School Finance, KDE, for it to be considered filed timely. No more than three (3) files total (text and spreadsheet) will be accepted electronically, unless alternate arrangements are made through the Division of School Finance.
- C. If necessary, ACCOUNTANT must file a request for extension, fully describing the reasons for the request. The request must reach the Division of School Finance by **October 17, 2005.**

II. DUTIES OF BOARD

- A. BOARD shall make available to ACCOUNTANT no later than August 1 all books, accounts, reports, vouchers, correspondence files, records, money, and property under its control which may be requested by ACCOUNTANT in the course of performance of the audit.

III. COMPENSATION

- A. ACCOUNTANT shall be paid an amount agreed upon between the auditor and district which is incorporated herein for the successful completion of the work defined by this agreement.
- B. Final payment is predicated upon completion of the work and delivery of documentation described in section DUTIES OF ACCOUNTANT of this contract.
- C. Compensation to ACCOUNTANT for any increase or decrease of audit scope by authority of Section V SUPPLEMENTAL AGREEMENTS of this contract must **be defined in said agreements and approved by COMMITTEE.**
- D. ACCOUNTANT shall submit to BOARD an invoice for payment which shall be signed by ACCOUNTANT and contain adequate supporting documentation such as: **detail of hours worked by each auditor classification (e.g., partner, manager, supervisor, senior, staff, etc.) in major audit areas or supervisory/administrative functions.**

IV. AUTHORITY OF COMMITTEE

- A. BOARD, ACCOUNTANT AND COMMITTEE agree:
 - 1. That COMMITTEE and the Kentucky Department of Education may examine work papers of ACCOUNTANT and may perform quality control reviews of the audit procedures utilized during the course of the audit;
 - 2. COMMITTEE and BOARD may prohibit the use of any subcontractor by ACCOUNTANT. During the term of the contract, no subcontractor shall be used without the prior written approval of COMMITTEE and BOARD; and
 - 3. COMMITTEE may allow for extension of time for completion and delivery of the audit report.

V. SUPPLEMENTAL AGREEMENTS

- A. If during the course of the audit a material exception is noted by ACCOUNTANT that requires additional procedures or an increase in the scope of the audit, the scope of the audit may be increased by written supplemental agreement of BOARD and ACCOUNTANT if the material exceptions have first been reported in writing by ACCOUNTANT to COMMITTEE. The scope of the audit may also be reduced by written supplemental agreement of BOARD and ACCOUNTANT if the reasons for the reduction have first been reported in writing by ACCOUNTANT to COMMITTEE.

VI. DELIVERY OF AUDIT REPORT

- A. ACCOUNTANT agrees to begin the audit of accounts of BOARD on or about August 1 or 15 days from execution date of this contract, whichever is later, and further agrees to complete and deliver a signed copy of the audit report to BOARD and to COMMITTEE and electronically submit the report to KDE on or before October 31.
- B. A written request for extension of time to deliver the audit report from ACCOUNTANT shall be received by the Division of School Finance, Kentucky Department of Education, on or before October 17. Requests for extensions will include but not be limited to the following information: length of extension, reason for extension, work completed to date, work to be completed and estimated release date of audit.
- C. Failure to request an extension will be grounds for the committee to impose penalties under VII.

VII. LATE PENALTIES

- A. There shall be a 10% reduction of the original audit fee if any of the following occur: (1) the electronic copy and the hard copy of the audit report are not delivered on or before October 31, or on the last day of any extension, (2) the audit report does not contain the information shown in Appendix I, Sections 7 and 10, and/or (3) the audit report is not submitted as referenced above in Duties of Accountant, Section I.B., unless alternate arrangements have been made with the Division of School Finance, KDE.
- B. ACCOUNTANT may be ineligible to conduct a school district audit for the upcoming fiscal year if any of the stipulations in section A occur.
- C. COMMITTEE may waive penalties for delays caused by circumstances beyond the control of ACCOUNTANT.

VIII. EFFECTIVE DATE

- A. This agreement shall not become effective until COMMITTEE has approved an application of BOARD for the audit and has approved this agreement.

IX. TERMINATION

- A. The BOARD shall have the right to terminate and cancel this contract at any time without cause upon 30 days written notice served on the ACCOUNTANT by registered or certified mail. The BOARD shall have the right to terminate and cancel this contract for cause upon 5 days written notice served on the ACCOUNTANT by registered or certified mail.
- B. If cause exists to terminate and the BOARD does not terminate, the COMMITTEE may terminate and cancel this contract for cause upon 5 days written notice served on the ACCOUNTANT by registered or certified mail.
- C. "Cause" includes, but is not limited to:
 - (a) failure to commence work within 15 days of execution of the contract or August 1, whichever is later;
 - (b) previous history of extension requests by the same ACCOUNTANT for the same district;
 - (c) failure to complete the contract by October 31;
 - (d) failure to communicate to the Department of Education in a timely manner problems encountered in conducting the audit.

Cause shall not include any factor wholly the fault of the BOARD.

X. CONFLICTS OF INTEREST

- A. ACCOUNTANT represents and warrants that (a) ACCOUNTANT is legally able to enter into contracts with BOARD, (b) the performance of this agreement would not violate any conflict of interest statutes, and (c) that ACCOUNTANT has no personal interest in the financial affairs of BOARD or any of its officers or employees.

AGREED TO BY:

_____ BOARD OF EDUCATION	_____ ACCOUNTANT
BY: _____ SCHOOL BOARD CHAIRMAN	BY: _____ FIRM
_____ SECRETARY	_____ PARTNER

STATE COMMITTEE FOR SCHOOL DISTRICT AUDITS

BY: _____
STATE COMMITTEE CHAIRMAN

APPENDIX I GENERAL AUDIT REQUIREMENTS

1. The State Committee for School District Audits requires all local school boards to have an annual audit of the fiscal records and accounts under the board's control. If the board members have also incorporated as a "Finance Corporation", that entity and related fiscal records and accounts are to be included in the audit.
2. The audit shall cover an entire fiscal year ending June 30 unless otherwise specified by the State Committee for School District Audits. If more than one year is audited, each fiscal year shall be reported separately.
3. Except in cases where special audits are authorized by the State Committee for School District Audits, the local boards of education shall select the auditor. Selection shall be made from the *Register of Kentucky Accountancy* published by the State Board of Accountancy of Kentucky.
4. Each local board of education shall make application for an audit on forms provided by the Division of School Finance, Kentucky Department of Education (KDE). **Three** copies of the contract forms shall be submitted, on or before May 16 of the fiscal year to be audited, to the State Committee for School District Audits for contract approval. **THE LOCAL BOARD OF EDUCATION DOES NOT HAVE A VALID CONTRACT WITH THE AUDITOR UNTIL THIS APPROVAL IS GIVEN.**
5. The audit shall be conducted in accordance with generally accepted auditing standards; *Government Auditing Standards*¹, issued by the Comptroller General of the United States; the provisions of *Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations*, and the audit requirements prescribed by the Kentucky State Committee for School District Audits in *Appendix I of the Independent Auditor's Contract - General Audit Requirements, Appendix II of the Independent Auditor's Contract - State Audit Requirements, and Appendix III of the Independent Auditor's Contract - Electronic Submission*.
6. The scope of the audit shall include but not be limited to:
 - (1) General Fund;
 - (2) Special Revenue Fund;
 - (3) Capital Projects Fund;
 - (4) Debt Service;
 - (5) School Food Service;
 - (6) Internal Service Funds;
 - (7) Activity Funds;
 - (8) Fiduciary Funds;

¹ *Government Auditing Standards* require participation of the auditor in an external quality review program and continuing education related to government auditing.

- (9) Fiscal Agent Funds; and
- (10) Fixed Assets as required by GASB 34.

If, in the course of field work, it is determined that funds have been transferred to a school through the school based council allocation process, those funds shall be considered Board funds, not activity funds, and audited as part of the general fund.

7. The report shall contain all reportable conditions, with those reportable conditions which are considered material weaknesses being appropriately segregated and identified. Reportable conditions presented as part of the report, as well as other matters conveyed in a separate management letter, shall be well developed and shall consist of the following components:
 - (1) A statement of condition(s).
 - (2) The criteria for the reportable condition(s).
 - (3) The cause of the condition(s).
 - (4) The effect of the condition(s).
 - (5) A recommendation for correction(s).
 - (6) Management's response to the recommendation.

Each management letter shall report on the status of previous management letter comments and the progress toward the resolution of concerns identified during the preceding audit.

8. One (1) copy of the report shall be submitted electronically in ² any of the following formats: Text documents shall be submitted in Microsoft Word, and /or Adobe Acrobat (PDF) format, spreadsheet documents are to be submitted in Microsoft Excel, and /or Adobe Acrobat (PDF) format along with one (1) signed paper copy for our file, to the Division of School Finance, KDE, no later than October 31 following the fiscal year end. The audit report will not be considered filed timely unless the Division of School Finance has received the electronic copy and the hard copy. No more than three (3) files total (text and spreadsheet) will be accepted electronically, unless alternate arrangements are made through the Division of School Finance.
9. The official records and reports of the school district shall not be taken from the board of education office during the course of the audit engagement.
10. Findings, questioned costs, management letter, Detailed High School Activity Fund Schedule(s) and responses to findings and the management letter shall be submitted as a part of the audit report. The High School Activity Fund Schedule should categorize each individual activity fund by account, reflecting all activity funds of the high school. Elementary and Middle School Activity Funds should be summarized in a single line per school.

² Appendix III.

11. One (1) copy of a bound audit report, along with the Data Collection Form, shall be submitted by the District, directly to the Single Audit Clearinghouse, as prescribed in OMB Circular No. A-133.
12. As stipulated in Statement on Auditing Standards (SAS) 78, an understanding of internal control activity must be sufficiently gained to plan the audit, assess risk, and determine the nature, timing, and extent of audit tests to be performed. Information system control activities must be considered to help ensure transactions are valid, properly authorized, and completely and accurately processed. Control activities to help ensure proper segregation of duties, logical and physical security, and disaster recovery should also be considered and tested.
13. The auditee is required by KDE to prepare a summary schedule of prior audit findings even if there are no matters reportable therein.

APPENDIX II

STATE AUDIT REQUIREMENTS

As part of the auditor's examination, the following procedures and tests are considered required. These are not intended to establish minimum audit procedures, but are listed to highlight their significance in a school district audit.

1. Examination of Board Minutes, Insurance Policies, Contracts, Bids, and Collateral - An examination of these documents shall be made insofar as they affect the financial transactions of the district and the district's compliance with statutes and regulations. Of special concern are adherences to bid laws, risk management, conflict of interest, and contract approvals.
2. Examination and Analysis of Sources of Income - Auditors having approved contracts with local boards of education receive a District Payment Register listing all payments to the district from the Kentucky State Treasurer. This report, sheriff's reports on tax receipts (sheriff's settlement), bond issues, interest recaps, and other documentation shall be used to verify and classify receipts. Auditors also receive health insurance, flexible spending account, life insurance, administrative fee, KTRS and Voc-ED information for their review.

The auditor shall also be concerned with the propriety of the allocation of tax receipts between the general and building funds.

3. Verification and Legal Authorization of Disbursements - Determine the propriety of disbursements on a test basis using the following documents:
 - a) Official minutes - (authorization);
 - b) Standard invoices (or reasonable facsimile);
 - c) Vendor invoices;
 - d) Orders of the Treasurer (or reasonable facsimile);
 - e) Cancelled checks;
 - f) Purchase orders (receiving slips, requisition forms);
 - g) Signed claims for reimbursement, advancements, etc.;
 - h) Payroll reports;
 - i) BG-1s (construction);
 - j) Interfund transfer forms (or reasonable facsimile);
 - k) Board orders;
 - l) Contracts and/or lease agreements; and
 - m) Board policy for pro rata allocation among funds and other board policy pertaining to disbursements.
4. Bonded Indebtedness (KRS 157.632) - The auditor shall confirm with the trustee the beginning balance, receipts, disbursements, and ending balance of each bond issue. The auditor shall determine if receipts were in agreement with amounts as specified in the pay schedules and if each bond account was reconciled for the period. The degree of

compliance shall be disclosed. The composite bond schedule shall be reviewed, including all information relative to the various issues.

Review any participation agreements between the board or the district finance corporation and the School Facilities Construction Commission (SFCC). The general wording of the agreement indicates the board is legally liable for the local portion and the SFCC portion of the bond issues. The total debt of the district shall be scheduled with the SFCC obligation segregated. The notes to the financial statements shall fully explain the agreement and debt.

5. Long-Term Leases - Examine any long-term lease agreements, lease-purchase agreements, or other multi-year funding arrangements for adherence to bid laws, payments being made from the proper fund, and terms and conditions meeting statutory requirements.
6. Budgets - A copy of the Tentative Budget and Working Budget, as adopted, with amendments, shall be given to the auditor at the beginning of the engagement. Comparison of actual income and disbursements with the budget may disclose fiscal management weaknesses or extraordinary events to be investigated. Full disclosure of findings is desired.
7. Accounts Receivable - Accounts receivable are recognized on the modified accrual basis of accounting. GASB 33 establishes general standards for the recognition of assets on the balance sheet (i.e., cash or accounts receivable) and the income statement (i.e., revenue). The asset recognition question arises when cash has not yet been received, and a determination must be made for recognizing the receivable as an asset on the balance sheet.

Pursuant to GASB 33, there are eligibility and timing requirements to consider. Transactions are eligible to be recognized when measurable and probable. Transactions such as state and federal mandated programs, grants and donations are recognized when all eligibility requirements are met. Property taxes are defined as imposed nonexchange transactions. Recognition of property taxes is based upon a timing requirement, which is "when enforceable legal claim and period for which is levied." Consistent with GASB 33, real property taxes levied as of January 1, 2005 but not yet billed will not be recorded as receivables on the balance sheet of Kentucky school districts as of June 30, 2005.

8. Accounts Payable - Accounts payable arise with the recognition of the liability of the school district to pay for goods received or services rendered, resulting in the identification of an asset or recording of an expense. Accounts payable are generally those liabilities whose liquidation is reasonably expected to require use of existing resources.

Because school districts must order supplies and equipment in the spring for the following school year, care should be taken to discern the amounts to be classified as encumbered rather than payable. The fund balance may be proportionately shown as

unreserved and reserved for encumbrances. Those purchase orders and contracts expected to be honored in the new year with new year revenue should be classified as encumbrances. No detail of encumbrances need be provided. The measurement accounts payable is principally from vendor invoices submitted to the school district for payment, from existing contractual arrangement, or from board orders.

9. Specific State Statute and Regulation Compliance Items - The Kentucky statutes and regulations contain many restrictions and requirements that school districts must follow. The auditor shall perform the necessary procedures to determine district compliance with the following items and any others that may come to their attention during the course of the audit.
 - a) Proper distribution of tax revenues to a restricted building fund account.
(See: Program Review 96-DFIN-157 Capital Construction Funding January 2, 1997).
 - KRS 157.440 authorizes the Facilities Support Program of Kentucky (FSPK) five (5¢) cent equivalent tax levy to qualify for School Facilities Construction Commission (SFCC) funding or state equalization. Use of funds is restricted to debt service, new facilities or major renovation listed in the approved facility plan. The required tax revenue is calculated by multiplying .0005 times the district's total property assessment including motor vehicles. In cases where a district has not collected all taxes due by June 30 because of late property tax bills, the amount due should be listed as receivable to the building fund account. The district's state equalization allotment is subject to the same restriction and must also be credited to the building fund account. A district that has not accepted an offer of assistance from SFCC and does not qualify for state equalization may use the revenue from the FSPK tax levy for any other school purpose with the approval of the chief state school officer.
 - KRS 160.476 allows a local board to set aside a portion of its local tax levy in excess of its FSPK levy for building purposes as outlined in the statute. Evidence of this levy may be obtained from the district's tax rates levied form or from board minutes.
 - KRS 157.621 allowed qualifying growth districts to levy a five (5¢) cent equivalent tax restricted to debt service and the construction of new facilities on the approved facility plan. The required receipts to the building fund may be calculated in the same manner as the FSPK levy. Evidence of this levy may be obtained from the district's tax rates levied form or from board minutes.
 - HB 269, the 2002-2004 Biennial Budget bill, authorized qualifying growth districts to levy an additional five (5¢) cent equivalent tax restricted to debt service and the construction of new facilities on the approved facility plan. This Equalized Growth Nickel qualifies districts for state equalization of the original growth levy. The required receipts to the building fund may be calculated in the

same manner as the FSPK levy. Evidence of this levy may be obtained from the district's tax rates levied form or from board minutes

- HB 269, the 2002-2004 Biennial Budget bill, authorized all districts to levy a Recallable Nickel, an additional five (5¢) cent equivalent tax restricted to debt service, new facilities, and major renovation of existing school facilities subject to voter recall. The required receipts to the building fund may be calculated in the same manner as the FSPK levy. Evidence of this levy may be obtained from the district's tax rates levied form or from board minutes.
- b) Support Education Excellence in Kentucky (SEEK) Capital Outlay and SFCC escrow (See: Program Review 96-DFIN-157 Capital Construction Funding January 2, 1997).
- KRS 157.420(4)-(6) provides that the SEEK Capital Outlay allotment is to be kept in a separate account (Fund 310) and used for debt service or capital outlay projects on the approved facility plan as evidenced by BG-1 forms. The required amount may be verified from the district's Final SEEK Calculation.
 - KRS 157.620 requires districts that accept a SFCC offer of assistance to restrict the Building Fund balance and the Capital Outlay Fund balance at the end of the odd numbered years to be used in accordance with the priorities of the districts' facility plans.
- c) Securance of a signed statement from each board member attesting that they have no knowledge of any conflict of interest or nepotism, as defined in KRS 160.180.
- d) Observance of approved single salary schedule (KRS 157.320(12) and 157.350(3); 702 KAR 3:070).
- "'Single Salary Schedule' means a schedule adopted by a local board from which all teachers are paid for one hundred eighty-five (185) days and is based on training, experience, and such other factors as the Kentucky Board of Education may approve and which does not discriminate between salaries paid elementary and secondary teachers. If the budget bill contains a minimum statewide salary schedule, no teacher shall be paid less than the amount specified in the biennial budget salary schedule for the individual teacher's educational qualifications and experience."
- e) Compliance with applicable laws and regulations governing procurement.
- School district purchasing procedures must comply with KRS 424.260 (Bid Law) unless they have adopted KRS Chapter 45A, the Model Procurement Code, by formal action of the board.³

³ Model Procurement has been adopted by more than half of the school districts.

- Bid Law KRS 424.260 and 702 KAR 3:135. The Bid Law requires districts to advertise for sealed bids for any contract, lease or other agreement for materials; supplies except perishable meat, fish and vegetables; equipment; or for contractual services other than professional, involving an expenditure of more than \$20,000. The \$20,000 threshold applies to district wide purchases rather than individual schools and is deemed to apply to items which can be purchased from the same vendor or can be grouped together by expenditure code such as teaching supplies.⁴ Contracts for construction of new school buildings and additions and repairs to existing buildings which exceed \$7,500 must be awarded by competitive sealed bidding (KRS162.070).
- Model Procurement Code (KRS Chapter 45A). The Model Procurement Code also requires that all contracts or purchases be awarded by competitive sealed bidding unless a determination is made by the board in writing that sealed bidding is not feasible. A brief summary of alternative purchasing procedures follows:

Competitive Negotiations (KRS Chapter 45A.370) are possible when specifications cannot be made sufficiently specific to permit an award on the basis of either the lowest bid price or the lowest evaluated bid price; sealed bidding is inappropriate because available sources of supply are limited; or the bid prices received through sealed bidding are unresponsive or unreasonable.

Noncompetitive Negotiation (KRS Chapter 45A.380) may be used when a written determination is made that competition is not feasible due to the following circumstances:

- 1) An emergency exists;
- 2) There is a single source within a reasonable geographic area of the product or service to be procured;
- 3) Contract is for professional services other than construction management services;
- 4) Contract is for perishable items purchased on a weekly or more frequent basis;
- 5) Contract is for replacement parts;
- 6) Contract is for proprietary items for resale;
- 7) Contract is related to selling by students as an educational experience;
- 8) Contract is related to authorized travel outside the school district;
- 9) Contract is for purchase of supplies for sale at public auction;
- 10) Contract is for group health and life insurance, worker's compensation and unemployment insurance;
- 11) Contract is for supplies which will result in a savings to the district

⁴ For example, a \$4,000 expenditure for like item from each of six school's activity funds would exceed the \$20,000 limit aggregated.

Small Purchase (KRS Chapter 45A.385) procedures may be used when the aggregate amount of the contract does not exceed \$20,000. Policy must be in writing and available to the public.

State Price Contracts (KRS Chapter 45A.420) may be used when the result is a savings to the district.

f) Conflict of interest as specified in KRS 156.480.

- No employee of a school district with decision-making authority over the financial position of a school, school district, or school system shall have any pecuniary interest in an amount exceeding twenty-five dollars (\$25).

g) Payment to the board of interest earned on investment of school tax revenues while in possession of the sheriff (KRS 134.140(3)(a)-(b)).

- If the sheriff invests local tax receipts, he must turn over to the board of education a proportionate share of interest earned.

h) Collection of School Taxes KRS 160.500-.510

- Tax collector is entitled to a fee equal to his expenses but not less than 1½% and not to exceed 4% for the collection of school taxes. The tax collector will, on or before the tenth day of each month, pay the depository of the board of education the amount of the school tax collected up to and including the last day of the preceding month. The amount paid, along with the classes of property from which it was received, is to be reported in writing to the treasurer of the board. This means that the sheriff or other property tax collector is not to deduct his fee from the taxes collected.

i) Board treasurer performing duties per KRS 160.560(2) and 702 KAR 3:080 related to approval of payments, bonding, check issuance and other duties.

- The treasurer shall execute an official bond for the faithful performance of his duties. This bond is to be guaranteed by an authorized surety company in an amount determined and paid for by the board of education. The treasurer receives all the money to which the board is entitled and deposits all funds into a designated depository. Withdrawal of such funds is only permitted with the proper order of the board. The treasurer is to keep a full account of all funds and prepare required reports.

j) Payments to substitute teachers per KRS 157.390, 156.160(1)(i), and 702 KAR 3:075.

- Boards of education shall adopt a per diem pay schedule for substitute teachers which will take into account their training and experience.

- k) Transportation of non-public school (private or parochial) children and reimbursement agreements per KRS 158.110 and accompanying attorney general opinions.
- l) Payment of salaries to school employees.
 - All school employees working on a continuing, regular basis shall be paid regularly on dates determined by the board of education during the school year or during the fiscal year for 12 month employees. (KRS 160.291 and 702 KAR 3:060)
 - KRS 161.011 requires that districts provide contracts for all classified employees and that job descriptions are consistent with KDE Classification Plan for Classified Employees.
- m) Publication of annual financial statement and budget.
 - KRS 424.220 requires that local boards of education publish annual financial statements which shall include the total amount of funds collected and received during the fiscal year from each individual source and the amount dispersed during the fiscal year to each individual payee and the purpose for which the funds were expended. The amount of salaries paid to district employees shall be shown as lump sum expenditures.
 - KRS 424.250 requires that local boards of education publish the tax rates levied by the district after approval by the Kentucky Board of Education.
- n) Extension of credit by the Board of Education as prohibited in Sections 177 and 179 of the State Constitution.
- o) Incompatibility of offices and employment as stated in Sections 165 and 237 of the State Constitution. Refer also to KRS 61.080, 160.180, and 160.345.
- p) Exceeding of budget per KRS 160.550.
 - No expenditures are permitted in excess of the income and revenue of any year.
 - A district is deemed to be deficit if it ends a fiscal year with a negative fund balance in the General Fund as reported on the district's Annual Financial Report.
- q) Per diem and expenses allowed board members (KRS 160.280).
- r) Adherence to budget cycle outlined in KRS 160.470, including allocations to school councils (KRS 160.345; 702 KAR 3:246).
 - KRS 160.470(5) states "within thirty (30) days after the district board of education has received its assessment data, the rates levied shall be forwarded to

the Kentucky Board of Education for its approval or disapproval. The failure of the district board of education to furnish the rates within the time prescribed shall not invalidate any levy made thereafter. KRS 160.345(2)(f) and 702 KAR 3:246 require local boards to make an allocation to school councils by March 1 of each year which shall include the amount for certified and classified staff based on the district's staffing policy and the amount for instructional supplies, materials, travel and equipment.

- KRS 160.470(6)(a) also requires boards of education to adopt a tentative working budget for the subsequent fiscal year by May 30 of each calendar year. The budget must contain a minimum 2% reserve based on the district's total budget. Evidence of board action can be found in the board's official minutes.
 - Finally, KRS 160.470(6)(b) requires local boards to adopt a final working budget and submit it for State Board approval by September 30 of each calendar year. Evidence of board action can be found in the official minutes of the board.
- s) Board designation of depositories of school funds and executed Bond of Depository per KRS 160.570(1) and 702 KAR 3:090.

“Each board of education shall appoint a bank, trust company, or savings and loan association to serve as its depository, and if its annual receipts from all sources exceed one hundred thousand dollars (\$100,000), it may designate three (3) depositories, except boards of education of school districts in counties containing cities of the first class may designate up to six (6) depositories. The depository may be designated for a period not to exceed two (2) years, and before entering upon its duties shall agree with the board as to the rate of interest to be paid on average daily or monthly balances.”

- t) Leases per KRS 65.944, 160.160 and 702 KAR 3:300.
- All leases in excess of \$100,000 must be reviewed by the Division of School Finance and approved by the Commissioner of Education. Technology lease agreements of any amount must be reviewed by the Division of School Finance and approved by appropriate personnel in the Department.
 - No board may lease a building or public facility that has been or is to be financed at the request of the board or on its behalf without approval of the Department.
- u) SFCC participation (KRS 157.611-640.)
- The School Facilities Construction Commission was established to help local school districts meet their school construction and education technology needs. The commission administers two separate programs: the school construction funding program and the education technology program. Funds appropriated for each program to the school district are to be maintained and audited separately.

- For the School Facilities Construction program, noncompliance of KRS 157.611(2), .615(1), .620(1-3), .622(5), .625(4), .627(1-3), or .632(1) shall be noted.
 - For the Education Technology Funding program, refer to KRS 157.650-.660 and Administrative Regulation 750 KAR 2:010. Expenditures from the technology fund must be consistent with the district's approved technology plan.
- v) Notification of Short Term Borrowing per KRS 65.7719.
- Local school districts may borrow money on short term basis subject to the restriction imposed by KRS 160.540.
 - KRS 65.7719 requires local school districts to notify the state local debt officer in writing prior to issuing notes for short term borrowing. Notification shall contain the terms of the notes, including the interest rates or method of determining rates, the approximate date of issue, the maturity dates, the trustee or paying agent, if any, and shall include a copy of the certificate of the governmental agency as to taxes or revenues to be collected during the term of the notes. No approval of the state local debt officer shall be required.
- w) Interest earned on Restricted Accounts per KRS 157.615 and KRS 157.620.
- The school district shall transfer all available local revenue, as defined by KRS 157.615(1), to a restricted account for school building construction, to be utilized for the priorities defined by the approved school facilities plan.
 - Interest earned on funds deposited in the restricted accounts required by KRS 157.620(2) section shall be deposited in the restricted account and shall become a part of the restricted funds.

The report on state compliance may be combined with the report on compliance with laws and regulations based on an audit of financial statements performed in accordance with *Government Auditing Standards* by including the following:

In addition, the results of our tests disclosed no instances of noncompliance of specific state statutes or regulations identified in *Appendix II of the Independent Auditor's Contract - State Audit Requirements*.

- x) Compliance with applicable statutes and regulations governing the Kentucky Teachers' Retirement System (KTRS) and the County Employees' Retirement System (CERS).
- y) Insurance required per KRS 160.105. The school district shall provide for fire & extended insurance coverage on each building owned by the board that is not surplus to

its needs as shown by the approved facility plan. This coverage must be an amount equal to the estimated replacement cost as provided in the attached memorandum, "Property Insurance Replacement Costs".

APPENDIX III

INSTRUCTIONS FOR COMPLETION AND ELECTRONIC SUBMISSION OF THE AUDIT REPORT

There must be one copy of the audit report, letters, notes, findings, and schedules submitted electronically. E-mail the reports to the following e-mail address:

Finrepo@kde.state.ky.us with “AUDIT” in the subject line (SUBJECT: AUDIT).

After the electronic copy is opened and reviewed, an e-mail will be sent confirming receipt.

SENDING AUDIT REPORT IN MICROSOFT WORD, AND/OR ADOBE ACROBAT (PDF):

- Complete the audit report, letters, notes, and findings.
- Send the report with the file name AUD<3-digit district code number>. 00 (or appropriate year) to the referenced e-mail address.

SENDING AUDIT REPORT IN MICROSOFT EXCEL, AND/OR ADOBE ACROBAT (PDF):

- Complete the audit report schedules.
- Send the report with the file name SCH<3-digit district code number>. 00 (or appropriate year)

IF YOU DO NOT HAVE ACCESS TO TO ADOBE ACROBAT OR MICROSOFT WORD OR MICROSOFT EXCEL:

- Call our office and alternate arrangements will be made; or
- Send the audit report and schedules on diskette.

ATTACHED IS THE DISTRICT CODE LISTING!!

Code	DISTRICT	Code	DISTRICT	Code	DISTRICT	Code	DISTRICT
1	Adair Co.	162	Fairview Ind.	391	Mason Co.	567	Walton-Verona Ind.
5	Allen Co.	165	Fayette Co.	392	Mayfield Ind.	571	Warren Co.
6	Anchorage Ind.	171	Fleming Co.	395	McCracken Co.	575	Washington Co.
11	Anderson Co.	175	Floyd Co.	401	McCreary Co.	581	Wayne Co.
12	Ashland Ind.	176	Fort Thomas Ind.	405	McLean Co.	585	Webster Co.
13	Augusta Ind.	177	Frankfort Ind.	411	Meade Co.	586	West Point Ind.
15	Ballard Co.	181	Franklin Co.	415	Menifee Co.	591	Whitley Co.
16	Barbourville Ind.	185	Fulton Co.	421	Mercer Co.	592	Williamsburg Ind.
17	Bardstown Ind.	186	Fulton Ind.	425	Metcalfe Co.	593	Williamstown Ind.
21	Barren Co.	191	Gallatin Co.	426	Middlesboro Ind.	595	Wolfe Co.
25	Bath Co.	195	Garrard Co.	431	Monroe Co.	601	Woodford Co.
26	Beechwood Ind.	197	Glasgow Ind.	435	Montgomery Co.		
31	Bell Co.	201	Grant Co.	436	Monticello Ind.		
32	Bellevue Ind.	205	Graves Co.	441	Morgan Co.		
34	Berea Ind.	211	Grayson Co.	445	Muhlenburg Co.		
35	Boone Co.	215	Green Co.	446	Murray Ind.		
41	Bourbon Co.	221	Greenup Co.	451	Nelson Co.		
42	Bowling Green Ind.	225	Hancock Co.	452	Newport Ind.		
45	Boyd Co.	231	Hardin Co.	455	Nicholas Co.		
51	Boyle Co.	235	Harlan Co.	461	Ohio Co.		
55	Bracken Co.	236	Harlan Ind.	465	Oldham Co.		
61	Breathitt Co.	241	Harrison Co.	471	Owen Co.		
65	Breckinridge Co.	242	Harrodsburg Ind.	472	Owensboro Ind.		
71	Bullitt Co.	245	Hart Co.	475	Owsley Co.		
72	Burgin Ind.	246	Hazard Ind.	476	Paducah Ind.		
75	Butler Co.	251	Henderson Co.	477	Paintsville Ind.		
81	Caldwell Co.	255	Henry Co.	478	Paris Ind.		
85	Calloway Co.	261	Hickman Co.	481	Pendleton Co.		
91	Campbell Co.	265	Hopkins Co.	485	Perry Co.		
92	Campbellsville Ind.	271	Jackson Co.	491	Pike Co.		
95	Carlisle Co.	272	Jackson Ind.	492	Pikeville Ind.		
101	Carroll Co.	275	Jefferson Co.	493	Pineville Ind.		
105	Carter Co.	276	Jenkins Ind.	495	Powell Co.		
111	Casey Co.	281	Jessamine Co.	496	Providence Ind.		
113	Caverna Ind.	285	Johnson Co.	501	Pulaski Co.		
115	Christian Co.	291	Kenton Co.	502	Raceland Ind.		
121	Clark Co.	295	Knott Co.	505	Robertson Co.		
125	Clay Co.	301	Knox Co.	511	Rockcastle Co.		
131	Clinton Co.	305	Larue Co.	515	Rowan Co.		
132	Cloverport Ind.	311	Laurel Co.	521	Russell Co.		
133	Corbin Ind.	315	Lawrence Co.	522	Russell Ind.		
134	Covington Ind.	321	Lee Co.	523	Russellville Ind.		
135	Crittenden Co.	325	Leslie Co.	524	Science Hill Ind.		
141	Cumberland Co.	331	Letcher Co.	525	Scott Co.		
143	Danville Ind.	335	Lewis Co.	531	Shelby Co.		
145	Daviess Co.	341	Lincoln Co.	533	Silver Grove Ind.		
146	Dawson Springs Ind.	345	Livingston Co.	535	Simpson Co.		
147	Dayton Ind.	351	Logan Co.	536	Somerset Ind.		
149	East Bernstadt Ind.	354	Ludlow Ind.	537	Southgate Ind.		
151	Edmonson Co.	361	Lyon Co.	541	Spencer Co.		
152	Elizabethtown Ind.	365	Madison Co.	545	Taylor Co.		
155	Elliott Co.	371	Magoffin Co.	551	Todd Co.		
156	Eminence Ind.	375	Marion Co.	555	Trigg Co.		
157	Erlanger Ind.	381	Marshall Co.	561	Trimble Co.		
161	Estill Co.	385	Martin Co.	565	Union Co.		